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Date: September 3, 2001
Priority: **Urgent**
Re: Washington, D.C. Foreclosure Law Effective Date

To People in the Servicing Community:

On Friday afternoon, August 31, 2001, Emergency rule making was promulgated by the Commissioner of the Department of Banking and Financial Institutions of the District of Columbia to implement the "Protections from Predatory Lending and Mortgage Foreclosure Improvements Act of 2000".

Under these regulations, the foreclosure process portions of the law apply to any foreclosure in which the first legal action (i.e., recording the foreclosure sale notice) occurs on or after October 1, 2001.

This will require significant changes in foreclosure process by the servicer. This is not a comprehensive list of the suggested changes; it is provided only to highlight the immediate issues and some of the more major concerns. If you have received this letter and you are not a servicer, please forward it to your servicer and outsourcer clients who have District of Columbia loans in their portfolios.

BREACH PROCESS

First and foremost, the servicer's breach process, if not already changed, needs to be changed immediately. Loans which are expected to have first legal action dates on or after October 1 must be properly breached now. A breach letter containing a thirty (30) day right to cure and other information is required in all cases. **This includes FHA and VA cases.**

The breach letter must contain the normal information contained in a standard breach letter, such as the amount needed and the date by which it must be paid. It must also state whether or not acceleration upon nonpayment is automatic, whether or not the addressee will have right to reinstate after acceleration, that the borrower/owner has the right to bring a court action to assert the non existence of a default or any other defense *"including the failure to send proper notices, to the acceleration and foreclosure sale."* There are no provisions

expressly authorizing a servicer to apply partial payments received without waiving acceleration.

Breach letters must be sent by certified mail, return receipt requested **AND** by regular mail **AND** by any other method set out in the deed of trust. If notice is not sent to a party entitled to notice, that party's rights are not affected until notice is sent, and any applicable response period passes.

A notice of acceleration is now required. The notice of acceleration may be contained in the breach letter. If it is, the letter **MUST** state the acceleration **WILL** occur if there is no cure. If the notice of acceleration in the breach letter is permissive or equivocal, a separate notice of acceleration must be sent.

At least during the transition period, a servicer should provide the foreclosure attorney with a copy of the breach letter and proof of mailing. If the attorney is obligated to send a separate notice of acceleration, the costs of the mailing will be added as a statutory cost, apart from any legal fees involved. This can be avoided by having an unequivocal statement of acceleration in the breach letter. A copy of a breach letter believed to be compliant is posted on The Fisher Law Group website at www.first-legal.com.

EXTENSIONS OF FIRST LEGAL ACTIONS

The requirement of a formal breach letter is new for FHA/VA loans. There are serious consequences imposed for failure to timely process these types of loans, e.g., the interest curtailment for missing a first legal action date in an FHA case. Since a servicer cannot take a first legal action until the breach period expires and since many servicers will not have already had these new breach processes in effect, servicers will probably have many cases in which the first legal action date will pass before the servicer can implement this new breach process and wait for a breach letter to expire. Servicers are advised to review their portfolios carefully and request extensions where appropriate.

This issue has been fully discussed with HUD officials in Washington. The issue is understood and it is likely that some kind of blanket extension will be granted under a mortgagee letter, but unless and until that happens, extensions **MUST** be requested.

Respecting loans that already require a breach letter under the terms of the loan documents, servicers should note (1) there is specific language required by the new law that is not required under the FNMA/FHLMC Uniform Instrument and (2) breach letters that previously were sent only by first class mail now need to be sent by both first class mail and certified mail. New breaches will likely be

required on many loans that have already been breached. While the servicer implements a compliant breach process and waits for breach letters to expire, first legal action dates may pass and the servicer will need to report these to the investor as an exception. Any loss because of this should be an investor loss, provided the servicer proceeds to implement change diligently. Servicers should not be held responsible for having previously implemented processes for changes in the law, when the regulators provided no lead time for implementation.

DOCUMENTS NEEDED FOR FORECLOSURE

Washington, D.C. is now an original document jurisdiction. All assignments, amendments and modifications are needed for the post sale audit process.

When a servicer refers a matter for foreclosure, the servicer will have to produce the original note or assure the foreclosure attorney that there is an original note that can be produced when needed. If the servicer provides assurance rather than the original note, the servicer needs to be right.

Under the new law, if the original note is lost or cannot be produced, prior to initiating foreclosure, the servicer must give written notice to the borrower/owner that note is missing and that attorney/trustee will be instructed to foreclose after 14 days have passed. The notice must contain an indemnity provision and notice to the borrower/owner of the right to petition court for further indemnity against multiple claims on the note. The failure to provide the original note will therefore increase costs by adding this new step to the foreclosure process. It will also cause a delay in foreclosure initiation.

If a servicer disregards this lost note process, believing it has or can obtain the original note later, it does so at its peril. If it turns out there is no available original note, this step cannot be made up later. The foreclosure sale will be invalid and a new foreclosure sale will be initiated. Obviously, therefore, the servicer is going to need to account for the original note at the time of referral.

Sometimes, a servicer does not have a copy of the note. It appears unlikely that a servicer will be able to foreclose using a power of sale process. Such a foreclosure will have to be judicial. It is difficult and perhaps not possible to prove the exact terms of the note without a copy of it and foreclosure may be unavailable.

Servicers will want to send copies of title insurance policies to their foreclosure attorney. If they do not, a full title will have to be ordered in all cases. A new requirement in the foreclosure process is the preparation and issuance of two title commitments. One is to be done as of the time of foreclosure initiation and one is

to be done at the time of audit. Since it is not known for whose benefit these commitments are issued and it is also not clear what liability there is for errors, most foreclosure attorneys will probably require full titles anyway.

PAYOFF AND REINSTATEMENT QUOTES

The new law requires payoff and reinstatement quotes to be provided within three (3) business days of a written request for them. There is no stated consequence but servicers will need to cooperate fully with the foreclosure attorney to meet this requirement.

REFERRAL REQUIREMENTS INVOLVING NEW PREDATORY LENDING PROVISIONS

The following is not an immediate problem. This is, however, a problem that may arise before the end of 2001.

It is possible that a deed of trust being foreclosed is dated on or after September 1, 2001, which does not have the disclosure forms discussed below attached to it, will need to be judicially foreclosed. The servicer can avoid this possibility ONLY if it can establish from its origination file that the loan was both applied for and accepted before September 1, 2001. The explanation for this is complicated.

The new law is very ambitious. In addition to being a foreclosure law, it is a codification of the law of mortgages, it is a reconveyance law, it is a settlement practices law and it is a predatory lending law. The predatory lending aspects are beyond the scope of this memorandum, but to need to be summarized.

A non-exempt "home loan" will be subject to the predatory aspects. Non exempt home loans will generally be subprime additional finance or refinances of residential property. After the effective date of the law, complex disclosure forms will have to be attached to the recorded deed of trust disclosing whether or not the loan is a non-exempt home loan. The content of those disclosure forms, in the absence of fraud, is binding on the parties.

If a deed of trust that is supposed to have these forms attached does not have them attached when recorded, the loan will have to be judicially foreclosed. If it does have them attached and the loan is a non exempt home loan, the borrower/owner will have the right to demand a judicial foreclosure. If it does have them attached and the loan either is not a home loan or is an exempt home loan, there is no right to demand judicial foreclosure. The foregoing assumes that the deed of trust has a power of sale. If it does not, judicial foreclosure is required.

In their wisdom, the regulators made the predatory aspects of the law applicable to all real estate loans “for which the application for the loan was submitted or accepted on or after September 1, 2001.” The regulations do not track the provisions of Section 205(a) of the Act, which provide for a sixty (60) day grace period after the effective date of the regulations for the use of the forms. It is not known whether the regulators intended for the grace period to apply or not, since they did not expressly use the language that would have been expected. (It should be noted that these are emergency regulations. The final regulations issued may clarify this.)

Submission or acceptance is an off-record event. The date either of those events happened is not in the public record and cannot be learned from a title search; the answers are in the servicer’s loan origination file. So servicers will need to provide this origination information on all deeds of trust dated after September 1, 2001 and not having the attached disclosure forms, in order to avoid the question as to whether a judicial foreclosure is required.

THE FOLLOWING IS IMPORTANT REGARDING THE ANY NON-EXEMPT HOME LOAN: If a loan is a non-exempt home loan, a servicer will need to provide the foreclosing attorney with the HUD1 from the origination file. The foreclosing attorney will be required to know the amount of any origination discount fees or points. The attorney will also need to know the status of both taxes and hazard insurance, including payment amounts and years covered. This is for calculating the amount of the “challenge” payment that the borrower/owner must pay in the event he or she asserts a right to judicial foreclosure. The amount of the challenge payment must be included on the Notice of Commencement of Foreclosure.

PENALTIES FOR FAILURE TO TIMELY RECONVEY

Servicers need to be aware of new provisions of the law respecting releases of satisfied deeds of trust.

To comply with the law, the release document must be sent to the Recorder of Deeds. The title company handling the settlement may request that it be sent to it instead. The servicer is required to include the recording cost of the release. The law does not say that this cost may be recovered by the servicer from the borrower, so the servicer who does not absorb that cost will do so at its risk. It is an open question.

The servicer has thirty days to provide a release. While the statutory language is unclear, the best reading of it is that, after thirty days, if no release has been provided, the borrower or title company can send another thirty day notice. After

the expiration of that thirty day notice, there is a delay fee of \$50 per business day not to exceed \$10,000. The borrower also has a legal action for all actual, direct and consequential damages caused by the failure to timely provide a release, as well as costs and expenses, including reasonable attorneys fees.

CONCLUSION

This is an overview of the servicing process changes required by this very ambitious law. It summarizes many provisions of the law and omits some details that a servicer would have to know to be in full compliance. However, it should serve the purpose of alerting servicers and getting them well on the way to implementing the necessary changes. It is not intended to be specific legal advice to any specific servicer. Servicers are cautioned to review this information with their foreclosure counsel, their regulatory counsel or their in-house counsel as appropriate.

The Fisher Law Group, PLLC is a full service law firm, providing foreclosure, bankruptcy, eviction and REO representation to investors and servicers in the District of Columbia and in Maryland. We are members of the MBAA. Please visit our website at www.first-legal.com for more information.

Please feel free to call me directly on extension 101 if you have any questions. You can also reach me at jfisher@first-legal.com.

Sincerely

JEFFREY B. FISHER

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